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November 14, 2002

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FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

**Bv Hand**

Marlene H. Dortch, Secretary  
Federal Communications Commission  
236 Massachusetts Avenue, N.E.  
Suite 110  
Washington, D.C. 20002

Re: *Petition for Rulemaking To Establish Revised Per-Call Payphone  
Compensation Rate, RM 10568*

Dear Ms. Dortch:

Please find enclosed for filing the original and four copies of the RBOC Payphone Coalition's Reply Comments in Support of Petition for Rulemaking in the above-captioned matter. Also enclosed is one extra copy of the reply comments. Please date-stamp and return the extra copy.

Thank you for your assistance. If you have any questions, please call me at 202-326-7921.

Sincerely,



Aaron M. Panner

cc: Qualex International

Enclosures

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**Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20554**

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NOV 14 2002

In the Matter of

Petition for Rulemaking To Establish Revised  
Per-Call Payphone Compensation Rate

R.M. 10568

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

**REPLY COMMENTS IN SUPPORT OF PETITION  
INTRODUCTION AND SUMMARY**

ORIGINAL

In its petition for rulemaking, the RBOC Payphone Coalition demonstrated that:

- Call volumes at average and marginal payphone locations have fallen by approximately half since the FCC set the per-call compensation rate, nearly four years ago;
- Per-station costs have generally remained approximately constant or have fallen slightly during the same period;
- The number of RBOC payphones deployed has fallen by more than 20% in the same period – an extraordinary decrease when one considers that the useful life of a payphone is 10 years;<sup>1</sup>
- The price that PSPs across the country typically charge for local coin calls has increased during this period from \$.35 to \$.50;
- As a result, callers using payphones to make local calls and other calls for which the rate is set by the market are subsidizing the country's long-distance carriers, who continue to pay for calls at an out-dated rate set well below the actual per-call costs of the payphone.

In their comments opposing the Coalition's petition for rulemaking (as well as a similar petition filed by the American Public Communications Council ("APCC")), the long-distance

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<sup>1</sup> See Second Report and Order, *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, 13 FCC Rcd 1778, 1802, ¶ 53 n.139 (1997) ("Second Report and Order").

carriers have disputed *none* of these facts. To the contrary, they generally acknowledge that, based on the Commission's D.C. Circuit-approved rate-setting methodology and current data, the per-call rate *should* increase significantly. *See, e.g.*, Comments of WorldCom at 1 ("Were the Commission to simply insert their estimated call volume into the formula it used to set the current \$.24 rate, the dial-around compensation rate would more than double."); Comments of Global Crossing at 2 (acknowledging that the Coalition and the APCC "want the Commission simply to utilize [the methodology from *the Third Report and Order*], but to update the inputs"). Such concessions prove the PSPs' point: the Commission cannot allow the current rate – which the long-distance carriers admit is not compensatory – to remain in effect. To do so would be to violate the plain language of section 276(b)(1)(A), which requires the Commission to ensure that PSPs receive fair compensation for each call made from their payphones. 47 U.S.C. § 276(b)(1)(A).

Nor do the long distance carriers offer any valid basis for delaying issuance of a notice of proposed rulemaking to update the per-call rate. First, they argue that the Commission should undertake a broad notice of inquiry to consider whether changes in the market warrant a change in the Commission's approach to setting the per-call rate. Such a broad inquiry, however, would be inappropriate. To be sure, PSPs must do business in ~~an~~ environment where the demand for the services they offer has been sharply reduced; as a consequence, the per-call costs of providing those services have increased, and the Commission should act immediately to ensure that the per-call compensation default rate reflects that change. But there is no evidence to suggest that the *structure* of the payphone market – that is, the manner in which PSPs do business and the basic services they offer – has changed, nor can the long-distance carriers claim that the assumptions and policy judgments underlying the Commission's *Third Report and*

*Order*<sup>2</sup> are any less valid today than they were in 1999. And while the long-distance carriers call for the Commission to investigate additional issues – service quality, public interest payphone deployment, subscriber fraud – they offer no justification for any Commission action on these issues, nor do they explain why investigation of any of these issues should delay Commission action on the per-call rate.

Second, the long-distance carriers argue that increasing the per-call default rate will further reduce demand for dial-around calls. But the long-distance carriers ignore the fact that by denying PSPs fair compensation on dial-around calls, the current default rate puts additional pressure on PSPs to increase market prices for other payphone services and/or to reduce the number of payphones deployed below the level that free-market demand would justify. PSPs must recover payphone costs from fewer callers; the purpose of the current petitions for rulemaking is to ensure that these costs are fairly borne by all payphone users. The long-distance carriers simply do not want to have to pay their fair share. Moreover, long-distance carriers consistently ignore the fact that the rate at issue here is a *default* rate, and PSPs and long-distance carriers are free to negotiate a lower rate if it is in their business interest to do so. Notably, however, by placing an artificial cap on compensation for dial-around calls and thereby suppressing revenues from these call types, the current default rate forces payphone deployment down – *and would do so even if market demand were sufficient to support current levels of deployment*.

Third, long-distance carriers dispute aspects of the calculations contained in the two petitions. These arguments go to the merits of the underlying issue and have nothing to do with

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<sup>2</sup> Third Report and Order, *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, 14 FCC Rcd 2545, 2571, ¶ 59 (1999) (“*Third Report and Order*”).

whether it is appropriate to issue the notice of proposed rulemaking. The Coalition's study – which is based on actual data from payphone operations comprising nearly two-thirds of the nation's total – are extremely reliable and consistent with the Commission's *Payphone Orders*. And the fact that the APCC's calculations independently yielded a closely comparable result provides further confirmation of the reliability of the Coalition's study.

The Commission should issue a notice of proposed rulemaking as soon as possible.

## **DISCUSSION**

The question before the Commission, at this preliminary stage, is a limited one: have the petitions for rulemaking filed by the Coalition and the APCC “disclose[d] sufficient reasons in support of the action requested to justify the institution of a rulemaking proceeding”? 47 C.F.R. § 1.407. There can be no serious question that they have. In adopting the current per-call compensation default rate, the Commission relied on cost data and call volume data collected between 1996 and 1998. Since that time, however, the volume of calls made from payphones has plunged – by more than 50%. Accordingly, the per-call rate set in January 1999 no longer “ensure[s] that each call at a marginal payphone location recovers the marginal cost of that call plus a proportionate share of the joint and common costs of providing the payphone.” *Third Report and Order*, 14 FCC Rcd at 2571, ¶ 59 (footnote omitted). The Commission should conduct a proceeding to update the rate based on current data. None of the comments filed in opposition to the Coalition's petition provide any basis for delay.

### **I. THERE IS NO NEED FOR A BROAD RE-EXAMINATION OF THE PAYPHONE INDUSTRY**

The Oppositions to Petition for Rulemaking argue that the Commission should undertake a broad Notice of Inquiry designed to re-examine the Commission's deregulatory policy governing the payphone industry. But the Commission need not and should not undertake any

such broad inquiry; it should simply address the fall in payphone call volumes by recalibrating the per-call rate to current conditions.

The Comments of WorldCom, Inc. are the most far-reaching in their call for the Commission to reconsider all of the work that the Commission already did in the series of orders that led to the adoption of the current default rate in the *Third Report and Order* (while likewise calling for the Commission to undertake an unprecedented central planning role for the industry). *See* WorldCom Comments at 6-18. The remaining Comments, while less detailed, are to the same effect. AT&T Comments at 4 (“The Commission should initiate a Notice of Inquiry to assess the changes that have occurred in the telecommunications market.”); ATX, *et al.*, Comments at 1 (“Commenters urge the Commission . . . to issue a Notice of Inquiry to obtain a complete and accurate picture of the payphone industry”); Sprint Comments at 7 (“the Commission . . . should issue a notice of inquiry”); Comments of IDT Corp. at 2 (“the Commission . . . should release a notice of inquiry”).

These calls for a broad-gauged investigation into the payphone industry are simply intended to delay the Commission’s action on the relatively straightforward issues presented by the petitions. Indeed, despite their rhetoric, the comments offer no basis to support the claim that the underlying structure of the payphone industry has changed in any way that would call the conclusions underlying the *Third Report and Order* methodology into question. The Commission found in the *Third Report Order* that “[p]ayphones offer access to a number of different services” (14 FCC Rcd at 2559, ¶ 30); that remains true today. The Commission found that “[t]he vast majority of the costs of providing payphone service are *fixed* costs that are *common* . . . to the provision of all payphone services” (*id.* ¶ 31 (footnote omitted)); that remains true today. The Commission found that “[b]ecause payphones have significant fixed costs that

must be recovered, the price for each type of payphone call must exceed the marginal cost of the call if the payphone is to earn a normal rate of return” (*id.* at 2560, 133 (footnote omitted)); that remains true today. The Commission’s observations concerning the cost structure of payphones and the nature of payphone competition (*e.g.*, *id.* at 2561-64, ¶¶ 34-39) remain valid and essentially unchallenged. And the basic policy judgments underlying the Commission’s establishment of a fair compensation rate – *i.e.*, the judgment that “consumers making one type of call, such as a local coin call, should not pay a higher amount to subsidize consumers that make other types of calls, such as dial-around or toll-free calls” (*id.* at 2570, ¶ 56) – not only remains an appropriate cornerstone of the Commission’s rate-making in this area, but it also underlines the urgency of action to correct the per-call compensation default rate.

The Commission’s analysis led directly to its conclusion that the default per-call compensation rate should be based on a bottom-up cost calculation that would permit PSPs to recover the marginal costs of a dial-around call plus a proportionate share of the joint and common costs of the payphone. This is precisely the methodology that the Coalition and the APCC urge the Commission to continue to employ. By contrast, the long-distance carriers suggest that the Commission should depart from this methodology without proposing any coherent alternative.<sup>3</sup> The sharp reduction in call volumes requires the Commission to recalculate the per-call default rate under its existing rules, but there is no reason for the Commission even to consider a *different methodology* when its current approach has been

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<sup>3</sup> Sprint proposes that the Commission adopt a “caller-pays compensation methodology.” See Sprint Comment at 6. The Commission rejected this proposal (for at least the second time) in the *Third Report and Order*. 14 FCC Rcd at 2597, ¶¶ 114-115; *see id.* ¶ 115 (“the statutory language and legislative history indicate Congress’s disapproval of a caller-pays methodology”).

approved by the D.C. Circuit and when the underlying structure of the industry remains unchanged.

Commenters also raise a series of irrelevant issues that are intended simply to delay action on the per-call rate. For example, several commenters claim that the Commission should look into “quality of service” issues. See WorldCom Comments at 11-12;<sup>4</sup> IDT Corp. Comments at 10-13. But there is no evidence whatsoever to suggest (1) that there is a need for the federal government to supplement states’ traditional role in regulating service quality (to the extent that any such regulation is even needed), (2) that any changes in the payphone market since 1999 make such an inquiry necessary, or (3) that a proceeding designed to update the per-call rate would be an appropriate proceeding in which to undertake such an inquiry. In fact, members of the Coalition are constantly working to maintain and improve service quality and to offer products and services that will appeal to consumers. There is absolutely no reason to believe that market forces – in this highly competitive market – will not address any service quality issues that might arise.

Other commenters argue that the Commission should investigate the possibility of fraud. See ATX, *et al.* Comments at 6-7; WorldCom Comments at 14. But the long-distance carriers offer no evidence that payphone fraud is widespread or that existing enforcement efforts are inadequate, and they likewise offer no reason to believe that the existence of such fraud could have any effect on the Commission’s policy governing payphone compensation. Accordingly, there is no place for this (non-) issue in this proceeding.

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<sup>4</sup> WorldCom even goes so far as to suggest that the Commission should inquire into the types of business activities that PSPs might undertake to supplement income and thereby “to stimulate usage and profitability.” WorldCom Comments at 11; see *also* TelStar Comments at 5-6. WorldCom cannot seriously maintain that central planners at a federal agency can do a better job than PSPs at investigating new business opportunities.



In addition, several commenters argue that the Commission should investigate the need for and policies to support public interest payphones. *See* TelStar Comments at 5; WorldCom Comments at 7. But, as the Commission first held in the ***First Report and Order***: the need for and establishment of public interest payphones is a separate issue from the treatment of payphones deployed by operation of the market. *See* 11 FCC Rcd at 20678-83, ¶¶ 277-286. Implementation of a public interest payphone program cannot take the place of carrying out Congress's requirement that the Commission adopt a compensation system that guarantees PSPs fair compensation for the services they provide. *See* 47 U.S.C. § 276(b)(1)(A); *compare id.* § 276(b)(2). Moreover, the Commission left the administration of public interest payphone programs to the states (*see First Report and Order*, 11 FCC Rcd at 20679, ¶ 280). There is no reason to believe that states have been unable to carry out that responsibility or that the Commission's wholesale intervention is warranted.

Accordingly, the Commission should – as the Coalition and the APCC have asked – simply issue a notice proposing an increase in the current per-call default rate without re-opening issues that the Commission has already successfully and finally resolved.

#### **11. CONCERNS ABOUT DECREASED DEMAND DO NOT JUSTIFY MAINTAINING THE CURRENT RATE**

The long-distance carriers argue that the current default rate should not be increased because to do so would suppress demand for payphone calls further. It is of course true that, all else being equal, an increase in price will tend to lead to a reduction in demand. But that observation provides no basis for delaying action on the Coalition's petition for several reasons.

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<sup>5</sup> Report and Order, *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, 11 FCC Rcd 20541 (1996) (“*First Report and Order*”).

First, the long-distance carriers ignore the fact that the question at issue here is whether, in light of the undisputed decrease in call volumes due to widespread proliferation of wireless phones, those who continue to use payphones for placement of dial-around calls should be subsidized by callers whose rates are set by the market. **As** the Commission has already concluded, the costs of the payphone are largely fixed costs that must be recovered from all payphone users. PSPs have already been compelled to increase the rates charged for other calls – most notably, the prevailing local coin rate has increased from \$.35 to \$.50 – since the current default rate was adopted. PSPs must recover their costs from a decreasing base of users. Denying PSPs fair recovery of costs on dial-around calls will simply increase the pressure on PSPs to raise other rates – suppressing demand for those other services further – and/or to eliminate payphones that would be self-supporting if the per-call compensation rate were updated to reflect current market conditions.<sup>6</sup> **As** the Commission has already held, long-distance carriers and their customers who choose to use payphones should bear a fair share of payphones’ costs, and, under the current default rate, they are not doing so.

Second, the long-distance carriers likewise refuse to acknowledge the fact that the rate the Commission sets will be a *default* rate, which applies only in the absence of an agreement between the PSP and the IXC. If, as the long-distance carriers claim, an increase in the compensation rate in line with costs would suppress demand enough so that total revenue from dial-around calls would decrease, not increase (and the Coalition does not believe this to be the

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<sup>6</sup> The Coalition’s study contradicts Global Crossing’s claim (at 3-4) that dial-around call volumes have fallen more than local-coin volumes. The Coalition has found that local coin call volumes have continued to make up approximately 60% of calls from RBOC payphones; the volume of 0+ calls has fallen most sharply; and dial-around calls make up an increased percentage of calls. This emphasizes the need to ensure that the dial-around rate accurately reflects per-call costs.

case), then the Coalition would have every reason to negotiate a different, lower rate with long-distance carriers. The reason that no such negotiation is possible now is that long-distance carriers have absolutely no incentive to pay anything more than the default rate set by the Commission. *See First Report and Order*, 11 FCC Rcd at 20567,749 (“uneven bargaining between parties necessitates the Commission’s involvement”). Indeed, PSPs worked for many weeks to negotiate with long-distance carriers a regulatory approach to the compensation issue that would provide the basis for a joint petition to the Commission. Long-distance carriers simply refused to entertain the idea of an increase in the current rate.

For related reasons, long-distance carriers’ claims that the Commission, rather than the market, should determine the appropriate level of payphone deployment is untenable. As an initial matter, the notion that the Commission can calibrate the per-call rate in order to achieve a particular level of deployment is unsupported and unsupportable – no regulator would have sufficient information to achieve that result. More important, it is for the market, not the Commission, to determine the appropriate level of deployment to meet market demand. The Commission can ensure that the market functions by increasing the default rate in line with current costs. If demand is sufficient to cover those costs, then payphone deployment will be maintained. If it is not, deployment may continue to decrease. Under the current rule, however, *payphone deployment would decrease even if demand were sufficient to support current levels of deployment* because the Commission’s default rate acts as an artificial cap on the rate that PSPs are permitted to charge for one type of service. Not only is increasing the default rate mandated by the terms of the statute and the Commission’s prior orders, but it is also desperately needed to ensure that the payphone market can function efficiently and respond appropriately to market demand.

### III. CHALLENGES TO THE PROPOSED COST STUDIES MUST BE RAISED IN THE RULEMAKING PROCEEDING

Finally, several parties raise challenges to specific aspects of the Coalition's cost study. AT&T's Comments are the most extensive and cover most of the issues raised in the remaining comments. The short answer to all of these challenges is that they provide no basis for delaying issuance of a notice of proposed rulemaking, because they do not tend to cast any doubt on the need for a proceeding to update the per-call default rate. These are issues that should be considered in the proceeding that a notice of proposed rulemaking would initiate.

In any event, AT&T offers no reason to doubt the reliability of the Coalition's study. (Indeed, even other long-distance carriers admit that, under the Commission's methodology, the per-call compensation rate would increase significantly in light of decreasing call volumes. *See* Comments of WorldCom at 1; Comments of Global Crossing at 2.) The sole issue that AT&T raises with respect to *methodology* relates to the Coalition's determination of call volume at the marginal payphone location. AT&T Comments at 15-16. But the Coalition has thoroughly explained this aspect of its study (see Coalition Petition at 5-6), and it is not "new" – it is the same methodology that the Commission itself used in the *Second Report and Order* and it reflects the market analysis that the Commission applied in the *Third Report and Order* as well.<sup>7</sup>

AT&T's remaining comments take issue with specific components of the Coalition study, but not only is the Coalition's study amply justified and documented, such quibbles plainly have no place in an opposition to a petition for rulemaking, where the question is whether

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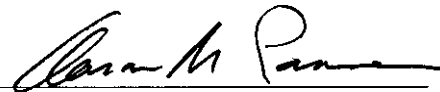
<sup>7</sup> AT&T also argues that the Coalition has made no allowance for the fact that some payphone locations do not recover their costs and that premises owners therefore pay for PSPs to deploy a payphone at those locations. *See* AT&T Comments at 16. AT&T is wrong. The Coalition included semi-public phone revenues – as well as other revenues, such as those from station advertising. *See* Coalition Petition at 9-10.

to initiate a proceeding. All the parties will have an opportunity to address the validity of the data included in the Coalition's (and the APCC's) cost studies; parties will likewise have the opportunity to offer their own data; and questions concerning any interpretive issues left open by the *Third Report and Order* can likewise be addressed. Indeed, it is precisely to ensure that the parties focus on these issues – and not submit irrelevant and unneeded comments addressing underlying issues that the Commission has already resolved – that the Commission's notice of proposed rulemaking should narrowly focus on the matter at hand: updating the per-call default rate to reflect current market data.

### CONCLUSION

The Commission should issue a Notice of Proposed Rulemaking proposing an increase in the per-call default rate to \$.49 per call.

Respectfully submitted,



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*Counsel for the RBOC Payphone Coalition*

November 14, 2002

## CERTIFICATE OF SERVICE

I hereby certify that, on this 14th day of November 2002, I caused copies of the RBOC Payphone Coalition's Reply Comments in Support of Petition for Rulemaking to be served by first-class mail (unless indicated by an asterisk) on the following parties:

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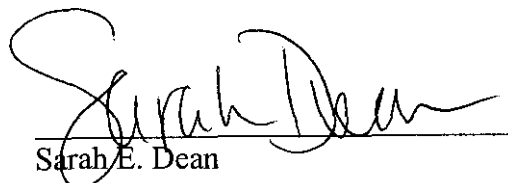
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